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365-510—69——1

In the Supreme Court of the United States

OCTOBER TERM, 1969

NORTHERN LINES MERGER CASE

No. 28

UNITED STATES OF AMERICA, APPELLANT

v.

INTERSTATE COMMERCE COMMISSION, ET AL.

No. 38

CHARLES E. BRUNDAGE, ET AL., APPELLANTS

v.

INTERSTATE COMMERCE COMMISSION, ET AL.

No. 43

CITY OF AUBURN, APPELLANT

v.

INTERSTATE COMMERCE COMMISSION, ET AL.

No. 44

LIVINGSTON ANTI-MERGER COMMITTEE, APPELLANT

v.

INTERSTATE COMMERCE COMMISSION, ET AL.

ON APPEALS FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF COLUMBIA

REPLY BRIEF FOR THE UNITED STATES

Despite the voluminous argumentation advanced by the appellees in their briefs, the issue in this case

remains simple and clear—whether preservation of rail competition is of little moment, or whether it shall remain an important element of railroad merger policy, one to be sacrificed only to satisfy a serious transportation need that cannot reasonably be met by less drastic means. The Interstate Commerce Commission and the merging lines contend that a merger of healthy parallel rail competitors who are dominant in their territory can be justified simply by predictions of savings, efficiencies and service benefits (ICC Br. 25–46; Northern Lines Br. 126–139). We contend, on the contrary, that the National Transportation Policy as applied to Section 5 of the Interstate Commerce Act values competition more highly. While preservation of competition in the transportation industries is not an unbending requirement, it remains nonetheless one of the fundamental desiderata in this as in other regulated industries, providing service and rate incentives that regulation alone cannot provide. We seek nothing more than a meaningful recognition and application of that policy in this case.[1]

There is relatively little in the many pages of the appellees' briefs relevant to the real question here

[1] The Commission's characterization of our position as one that would allow a merger only where it is necessary to rescue a failing but essential carrier (*e.g.*, ICC Br. p. 27) does not reflect a fair reading of our brief. Nor do we seek to displace the ICC's expert judgment as to what might be an appropriately important transportation need in any particular situation. We do urge that, at the very least, the Commission must make such a judgment, which it has not made and could not make on the record in this case.

that is not amply answered by our presentation in the main brief for the United States. The bulk of the opposing briefs simply rehashes and embellishes the Commission's Second Report and the underlying record, minimizing the competitive losses and maximizing the asserted benefits of the merger. If the purpose of the appellees is to convince this Court that the merger would not result in a serious loss of competition or that it would in fact produce important public benefits in an area of serious transportation need, or both, our answer is simply that—as we have shown in our main brief—the Commission has not so found. Rather, the Second Report, together with those portions of the First Report that are uncontradicted by the Second Report, amounts to an acknowledgement by the Commission, which cannot be contradicted on this appeal, that a substantial competitive loss is at stake and that it is not offset by any countervailing serious transportation need or other important public benefit. Accordingly, the appellees' elaborate discussion of the facts relating to competition and alleged benefits requires only a brief reply.

Apparently recognizing the inconsistency of seeking to support the Commission's order by what amounts in large part to impeaching its findings of fact on the competitive effects issue, the Commission's general counsel in his brief seeks to minimize the issue by arguing that rail competition in general and particularly in this case is unimportant and therefore should be given little weight (ICC Br. pp.

56–83). This new approach—which is at odds with what the Commission and the court below said, though it fairly reflects the hostility to competition implicit in the Second Report—raises problems of evident importance, and accordingly we shall discuss it first.

I

The general counsel's disparagement of rail competition is surprising and seems out of place in this litigation. It is not based either on findings in the examiner's report or in either of the Commission's two final Reports and thus cannot be advanced here; it appears to be a case of "*post hoc* rationalization" by counsel.[2] *Burlington Truck Lines* v. *United States*, 371 U.S. 156, 168–169; *Securities and Exchange Commission* v. *Chenery Corp.*, 318 U.S. 80, 87. And it is fundamentally inconsistent—as we have shown in detail in our main brief—with the line of authority in this Court reflecting Congress' intention that competition should remain a basic consideration in any restructuring of the rail system.

The Commission's brief argues that the oligopolistic structure of railroading and the mutual dependence

[2] The argument of the Commission's counsel appears to track closely the report of the hearing examiner on the proposed Milwaukee-Chicago & North Western merger, I.C.C. Fin. Dkt. Nos. 24182, et al., now pending before the full Commission on exceptions to the report. The Department of Justice has submitted a brief in that proceeding which challenges the examiner's competitive analysis but also states that the United States does not oppose that merger provided certain conditions are adopted.

created by limited trackage restricts the significance of competition. Yet competitive pressures even in an oligopolistic framework are strong and pervasive—as reflected by the Northern Lines' response to the Milwaukee's fast transcontinental train (App. 82). The more sellers, even in an oligopolistically structured transportation market, the less the likelihood that uniformity can be maintained under all the varied pressures of the American economy. That is why four is better than three, three better than two and two better than one.[3]

Nor does the "force of regulation" (I.C.C. Br. p. 57) minimize the role of competition. Regulation becomes inimical to competition only when it is con-

[3] "[A] three-person game is very fundamentally different from a two-person game, a four-person game from a three-person game, etc. The combinatorial complications of the problem * * * increase tremendously with every increase in the number of players * * * Whenever the number of players, i.e. of participants in a social economy, increases, the complexity of the economic system usually increases too; e.g. the number of commodities and services exchanged, processes of production used, etc." J. Von Neumann & O. Morgenstern, *Theory of Games and Economic Behavior*, 13 (3d ed. 1953). This principle was implicit in this Court's decisions under the Sherman Act in such railroad merger cases as *Northern Securities Co.* v. *United States*, 193 U.S. 197; *United States* v. *Southern Pacific Co.*, 259 U.S. 214; *United States* v. *Union Pacific R.R. Co.*, 226 U.S. 61, all of which emphasized the importance of preventing intensification of the railroad industry's monopolistic tendencies. The grant of antitrust immunity in present law has not changed the economic facts or diminished the value of rail competition; all it has done—as we show in our main brief—is to authorize the Commission to allow a rail merger with anticompetitive effects if there is a strong countervailing transportation need for the merger.

ducted to protect the regulated instead of the public. Railroads are not regulated in order to minimize competition, but to compensate for the concentration of economic power which all recognize to be unavoidably inherent in the industry. This makes all the more important the preservation of the competitive structure which does exist.

The regulatory scheme of the Interstate Commerce Act is, with some rarely invoked exceptions, basically permissive in nature. It depends primarily upon the initiative of railroad managements to propose innovations in rates and routes, service, and car supply and reductions in operating costs.[4] Even in rate making, there is a competitive zone of reasonableness in which each carrier is free to adjust charges for itself. *United States* v. *Chicago, M., St. P. & P. R. Co.*, 294 U.S. 499, 506. The importance of such rate competition is recognized in the Reed-Bulwinkle Act, 49 U.S.C. 5b, which, although designed to modify the preexisting prohibition against collective rate making (see *Georgia* v. *Pennsylvania R. Co.*, 324 U.S. 439), expressly guarantees each carrier's "free and unre-

[4] This is reflected, for example, in the Commission's insistence on the limited scope of its powers to compel joint rates and through routes (I.C.C. Br. 87, n. 26), or to require improvements in the quality of passenger service (*Adequacies—Passenger Service Southern Pacific Company between California and Louisiana*, 335 I.C.C. 415). Even when it uses its compulsory powers it generally adheres to arrangements voluntarily adopted by the railroads themselves. Thus in adopting new rules to alleviate the national car supply shortage, it simply made compulsory the long-standing rules of the Association of American Railroads (*Investigation of Railroad Freight Car Ownership, Car Utilization, Distribution, Rules and Practices*, 335 I.C.C. 264, 292).

strained right to take independent action," a right frequently resorted to under competitive pressures. Indeed the significance of rate competition is underlined by the emphasis of the proponents here on their contention that the merger conditions will at last make the Milwaukee into a true transcontinental rate making railroad.

There is no more reason, or support in the record, behind the Commission's arguments—which were made in part in the Second Report—that rail competition in the Northern Tier in particular is relatively unimportant. We have already shown in our opening brief the fallacy of contending that there is no real transportation competition as to shippers located on only one of the merging lines (U.S. Br. pp. 43–44). Market competition between a shipper located on one line and another shipper located on another does in fact operate to induce each carrier to protect its shipper customers from excessive transportation costs by keeping rates low and service good. And it is similarly fallacious to argue that competition for markets outside the Northern Tier is primarily with shippers in other parts of the country (ICC Br. pp. 66). There remains highly significant competition among shippers in the Northern Tier for such markets elsewhere; the merger would deny these shippers the benefits of competition in the transportation service upon which they depend for their access to those markets.

The merging lines and the Commission lay great stress upon the support for the merger advanced by

various shipper groups. As the hearing examiner recognized, however, this support was the product of an intensive public relations effort by the merging lines (App. 746), and much of the testimony was simply a reiteration of a brochure furnished by the carrier (see U.S. Br. p. 60, n. 46). Moreover, the very fact that a substantial number of shippers are wholly dependent on one of the merging lines for their rail service substantially reduces the value of their testimony, since they dare not offend the carrier.[5] Indeed the recognition of competition which many shippers admitted was disclosed only on cross-examination by counsel for the Department (I.C.C. Brief, pp. 80–81, n. 23; see record citations, Br. for United States at pp. 60–61). Certainly a poll of incompletely informed shippers subject to strong carrier pressures is no substitute for careful economic analysis by the Commission of the competitive effects that the merger would have.

With respect to the impact of intermodal competition, there is nothing in counsel's sampling of the record that can now contradict the Commission's own undisturbed findings in the First Report (ICC Br. 69–76; Northern Lines Br. pp. 102–114; see U.S. Br.

[5] Professor Karl M. Ruppenthal, Director of the Transportation Management Program at Stanford University has observed:

"[M]ost likely [a shipper] will have personal feelings about the merger proposal, but he will keep them quietly to himself. He does this because he does not wish to be on the losing side. He is all too apprehensive that there may be retribution in one form or another, particularly if he is especially dependent upon a single carrier for much of his transportation service." Traffic World, October 8, 1966, p. 44.

pp. 45-49). The gross figures relied on by the proponents to show a substantial growth in motor carrier traffic do not define the extent of actual diversion from the railroads or distinguish between traffic which a growing economy would allocate in all events to the motor carriers, and traffic which, while best suited for rail movement, has been lost because of avoidable service inadequacies.[6] And as the First Report observed, fluctuations in railroad revenues do not correlate with the rise of other modes of transportation. Rather they respond to fluctuations in the general level of economic activity (App. 137).[7]

Perhaps the most convincing evidence of the continued significance of rail competition lies in the fierce contest among the railroad intervenors in this case over conditions to protect them from feared diversions of traffic. While that struggle does not demonstrate that the other lines will substitute for the competition lost in the Northern Tier by this merger, it does answer Commission counsel's disparagement of rail competition.

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[6] Indeed, the Northern Lines' railway operating revenue showed a substantial improvement between 1958 and 1965. Great Northern's railway revenues were $251.7 million in 1958, declined somewhat in the early 1960s, but had climbed to $265.6 million by 1965. Northern Pacific had revenues of $179.1 million in 1958, a similar decline, and a climb to a peak of $197.9 million in 1965. The Burlington followed a similar pattern with revenues in 1958 of $258 million and in 1965 of $270.4 million (App. 80).

[7] Figures recently cited by the Commission reflect that Class 1 railroad revenues from freight in 1964 ($8.4 billion) were only one percent less than in 1955 (8.5 billion). *Investigation of Railroad Freight Car Ownership, etc., supra*, 335 I.C.C. 264, 272.

In short, there is no basis for counsel's effort in this Court to minimize the legal significance of the undisputably serious loss of rail competition in the Northern Tier that would result from the merger. And we shall show in the section that follows the weakness of the proponents' attacks upon the Commission's own measures of the rail competition that will be lost in the Northern Tier.

II

The Commission and the Northern Lines in their briefs make elaborate efforts to demonstrate that even if rail competition is important in the Northern Tier the amount of such competition that the merger would eliminate is less than our brief and the First Report say it would be. In large part, these discussions are belated attacks upon the measures of rail competition used in the First Report, offered without regard to the Commission's failure to make contrary findings in its Second Report. The appellees also place new emphasis upon competition from the Canadian and central transcontinental lines that is largely unsupported by any findings in the administrative proceeding. Much of what they say is quibbling over matters irrelevant to the real issue in this case; even if the arguments were taken at face value, they would not impair the conclusion of the First Report that there would be a very substantial loss of rail competition between the Northern Lines. This appeal is not an exercise in precise measurement of competition; rather the issue is

the relative weight that should be given to indisputably substantial anticompetitive effects. Nonetheless, some aspects of the appellees' discussions of competitive measures may warrant brief response.

The proponents' emphasis on alleged competition from other lines has practically no support in the Commission's opinions. Neither the discussion of this competition in the Second Report (App. 312–323) nor the hearing examiner's discussion of intramodal competition (App. 770–776) discloses the volume of traffic which might be affected by competition from the Canadian route. The only measure of central route traffic in the Commission's findings is a 1964 figure indicating that at representative northwest gateways the Union Pacific carried some 26.9 percent, compared with the Northern Lines' 61 percent and the Milwaukee's 12.1 percent (App. 146). And the First Report concluded, without contradiction in the Second Report, that "competition from Canadian transcontinental lines or the circuitous routes of the Southern Pacific would be generally ineffective * * *" (App. 146).

The present attack on the First Report's finding that competition between the merging lines would be eliminated at points originating more than 43 per cent of their freight revenues is supported neither by the Second Report nor by the examiner's findings (ICC Br. pp. 48–53; Northern Lines Br. pp. 82–86; see U.S. Br. pp. 9, 41–45). On the contrary, the Second Report expressly adopted the First Report's figures derived from Exhibit 16 (Tr. 10953, Exhs. 177, 178) that 6.16% of the North-

ern Lines' revenues in the Northern Tier derive from Class 1 stations and that 37.71% derive from Class 2 stations (App. 316); there was no rejection of these figures on the ground of double counting.[8]

[8] Class 1 stations are stations commonly served by two of the applicant carriers and no other rail carrier: Class 2 stations are stations commonly served by two of the applicant lines and at least one non-applicant line; Class 3 stations are served by one applicant only; and Class 4 by one applicant line and one or more other rail lines (App. 141).

At the time Exhibit 16 was introduced by applicants' sponsoring witness, he testified that "the double count as to cars, tons and revenues for such shipments [*i.e.*, shipments in the Northern Tier] thus reflects the competitive situation at both the originating and terminating stations" (Tr. 503). Only after this approach backfired did the merging lines, in their petitions for reconsideration, protest the double count by suggesting that only traffic *originating* from Class 1 and Class 2 stations in the Northern Tier should be considered, without regard to traffic terminating on their lines. But if the Exhibit 16 figures are analyzed to show both traffic originating and terminating at competitive points it can be demonstrated that the common points in the four-state area account for 70.22 percent of the gross revenue from terminated traffic, 57.3 percent of the total terminating tonnage and 60.57 percent of the termination of cars. A comparison of terminated and originated traffic indicates that the applicants terminate about 75 percent as much traffic as that originated. And whether originated or terminated traffic is taken into account, overhead traffic must be added.

One can make calculations from the Exhibit 16 data that are more precise than the above, and also eliminate double counting. Following the applicants' emphasis on originating traffic, one can calculate (a) traffic originating at GN-NP common points, and add to that (b) interline traffic terminated at a common point. This eliminates the double counting of traffic terminating at local points which also originated at local points. The resultant percentages would be about 33 percent for revenues, 23 percent for tonnage, and 31 percent for

The balance of the Second Report's discussion of Northern Tier competition appeared in one sentence, which simply confirmed the obverse of the figures just stated (App. 317); thereafter the discussion was directed to the system-wide effects of the merger including the vast and non-competitive Burlington territory. Thus the Commission simply did not adopt the analysis now belatedly offered by its counsel and by the Northern Lines. Nor did it make any finding reducing the significance of overhead traffic, which the First Report found to represent some 12 percent of the merging lines' revenues. Thus, taking account of the findings which the Commission adopted and the evidence supporting them, rather than counsel's attempt to supply new findings, the drastic competitive impact of the merger is plain.

In measuring the loss of competition, almost any statistical representation is of course imperfect. Competition has indirect effects which cannot be measured but can only be recognized from the availability to shippers of various choices with respect to the origination, routing and termination of traffic. As the Commission observed in its First Report, "anticompetitive consequences of the merger would not be

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cars. Or, one can make a calculation emphasizing (a) terminating traffic, including traffic terminating at common points, plus (b) traffic originating at common points and moving beyond applicants' lines. The resultant percentages would be about 52 percent of the Northern Lines' revenues, 36 percent of their tonnage, and 43 percent of their cars.

The foregoing calculations are derived from data included in Exhibit 16, as shown in the Appendices to this brief.

confined to stations where applicants are directly competitive. Today, rate innovations and service improvements by one of the Northern lines create strong pressure from the shippers for similar treatment by the other. These indirect benefits of competition between the Northern lines cannot be measured statistically but they are real." (App. 150.)

III

The arguments that are made to support the Commission's approval of the vast Northern Lines merger (reversing its earlier contrary view) are, when added together, rather remarkable. The Great Northern and the Northern Pacific—both strong and healthy carriers with longstanding "substantial common interests and interlocking relationships" (Northern Lines Br. p. 4)—insist that unless they merge they cannot protect themselves from each other or even from themselves; the inexorable requirements of competition and the apparently irresistible urge to protect their individual long hauls in every situation prevent them from cooperating as separate entities to exchange trackage rights, interchange and pool equipment, and arrange through-routes, even where the consequence would be to increase their own profits, improve the services given their shippers, and prevent diversion of traffic to other modes.[9] At the same time, the

[9] The Commission's First Report made the pertinent suggestion that the hope for a mutually profitable merger may have been a strong incentive for the Northern Lines not to undertake otherwise sensible coordination, and that such improvements could be expected if the merger were not approved (App.

Commission is arguing that railroad competition is an insubstantial thing because the structure of the industry and its inherent nature forces "a high degree of concentration and agreement among the few" (ICC Br. p. 57). And in the next breath, the Commission seeks to justify the merger as a "vehicle for the imposition of conditions which would remove [the Milwaukee's competitive] handicaps and in the Commission's view, convert Milwaukee into a transcontinental competitor" (ICC Br. p. 85). Therefore, we are told, it is necessary to create a near monopoly of rail transportation in the Northern Tier. And even a group of shippers agrees that their only hope of escaping managerial practices of the Northern Lines which separately deny them adequate service is to join those managements into one.

The role of the Milwaukee in the proponents' argument involves a set of paradoxes all its own. First, one might consider it anomalous to advance as a prime justification for a merger of vast scope the fact that it would be possible to attach a useful condition as an incident to its approval. And the paradox is multiplied when it is considered why the Milwaukee conditions are desirable in the first place. It is plain from the record in this case that the Milwaukee's problems as a transcontinental railroad stem from the refusal of its two giant competitors, the Northern Lines, to enter into joint rates and through routes

164). Its counsel now urges that rail mergers are necessary because the "record of American railroads in voluntarily effectuating apparently sensible and economic coordinations is not encouraging" (ICC Br. pp. 97–98).

with it and their efforts to impose every restriction possible in order to short-haul it. The Commission has taken no steps to help the Milwaukee escape this strangle hold. But now we are told that the Commission must grant the Northern Lines' request to increase their dominance because that is the only way that the Northern Lines can be persuaded to agree to stop abusing the dominance they already have.

In brief, the Commission has acceded to a serious loss of rail competition that is justified by little more than the prospect that the merger parties will cease their efforts to injure the Milwaukee and the hope that together their managements will improve upon the shortsighted and inefficient practices that they have followed separately. We submit that the Commission's action upon the substantially undisputed facts of this case violates the public interest standard of Section 5 of the Interstate Commerce Act and is inconsistent with the National Transportation Policy.

This case will not only shape the first crucial stage in the restructuring of the transcontinental rail system in the West but also will necessarily determine the role that competition will play in the future of the nation's rail system as a whole. The Commission's approach to the fundamental problems before it should not be allowed to stand.

CONCLUSION

For the foregoing reasons and those stated in our main brief, the judgment of the district court should be reversed and the case remanded to the Commission.

Respectfully submitted.

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APPENDIX I

NORTHERN LINES CARS TERMINATED IN THE FOUR STATES

[Thousands omitted]

	Total cars (all 4 classes)	Class 1		Class 2		Subtotal (classes 1 and 2)	
		Cars	Percent of total	Cars	Percent of total	Cars	Percent of total
Minnesota	271	29	10.70	142	52.40	171	63.10
Montana	91	26	28.57	3	3.30	29	31.87
North Dakota	76	18	23.68	16	21.05	34	44.73
Washington	338	5	1.48	231	68.34	236	69.82
Total	776	78	10.05	392	50.52	470	60.57
Less CB&Q	15	5	.....	4	.....	9	.....
	761	73	9.59	388	50.99	461	60.58

NORTHERN LINES TONNAGE TERMINATED IN THE FOUR STATES

[Thousands omitted]

	Total tons (all 4 classes)	Class 1		Class 2		Subtotal (classes 1 and 2)	
		Tons	Percent of total	Tons	Percent of total	Tons	Percent of total
Minnesota	11,458	1,065	9.29	5,742	50.11	6,807	59.40
Montana	3,809	1,029	27.01	68	1.79	1,097	28.80
North Dakota	3,151	954	30.28	529	16.79	1,483	47.07
Washington	12,468	200	1.60	8,113	65.07	8,313	66.67
Total	30,886	3,248	10.52	14,452	46.79	17,700	57.31
Less CB&Q	485	167	.....	115	.....	282	.....
	30,401	3,081	10.13	14,337	47.16	17,418	57.29

NORTHERN LINES REVENUES FROM THEIR TERMINATIONS IN THE FOUR STATES

[Thousands omitted]

	Total revenue (all 4 classes)	Class 1		Class 2		Subtotal (classes 1 and 2)	
		Revenue	Percent of total	Revenue	Percent of total	Revenue	Percent of total
Minnesota	56,870	5,032	8.88	39,949	70.25	45,001	79.13
Montana	19,528	5,482	28.07	1,252	6.41	6,734	34.48
North Dakota	17,080	4,701	27.52	3,203	18.75	7,904	46.27
Washington	84,415	1,159	1.37	64,105	75.94	65,264	77.31
Total	177,893	16,394	9.22	108,509	61.00	124,903	70.22
Less CB&Q	2,616	1,349	.....	639	.....	1,988	.....
	175,277	15,045	8.58	107,870	61.54	122,915	70.13

Source: Exhibit 16.

APPENDIX II

COMPARISON OF TERMINATED AND ORIGINATED TRAFFIC IN THE FOUR STATES

[Thousands omitted]

	Cars originated	Cars terminated	Percent cars terminated of cars originated
Minnesota	432	271	62.7
Montana	159	91	57.2
North Dakota	100	76	47.5
Washington	338	314	93.0
	1,067	776	73.0

	Tons originated	Tons terminated	Percent tons terminated of tons originated
Minnesota	24,313	11,456	47.1
Montana	6,763	3,809	56.4
North Dakota	7,079	3,151	44.5
Washington	11,361	12,466	109.9
	49,517	30,886	62.5

	Revenues from originations	Revenues from terminations	Percent revenues from terminating traffic of revenues from originating traffic
Minnesota	$43,694	$56,870	130.2
Montana	59,803	19,528	32.6
North Dakota	41,940	17,080	40.8
Washington	77,557	84,415	108.7
	$223,086	$177,893	79.8

Source: Exhibit 16.

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